II. THE COMMISSION SHOULD RECLASSIFY LEC PAYPHONE ASSETS AS CPE IN A MANNER CONSISTENT WITH COMMISSION PRECEDENT

As the Coalition pointed out in its initial comments, the Commission consistently has used net book value when reclassifying LEC assets. Urging the Commission to depart from this unbroken historical practice, various commenters have presented various alternatives. The schemes proposed by these commenters, however, would mire the Commission in an endless stream of impossibly subjective judgments about the valuation of LEC payphone assets. CPA, for instance, calls on the Commission to look beyond net book value to the "[t]he going concern value of LEC payphone operations," which allegedly "exceeds the heavily depreciated net book value of their equipment." CPA at 17 & n.17. But net-book value is not too low, and such a valuation scheme would require the Commission to make arbitrary judgements about the value of payphone assets in any event. Under such circumstances, the Commission has previously "us[ed] net book value as a proxy for economic value," noting that it "has the advantage of extreme simplicity."[16]

Simplicity is conspicuously lacking from the comments of the Georgia Public Communications Association ("GPCA"), which proposes to auction off RBOC payphone assets, with the RBOC to have the option of matching the highest bid. This preposterous proposal would essentially condemn all the RBOCs' payphone assets without an iota of statutory support.

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[16]Report and Order, Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services (Second Computer Inquiry), 95 F.C.C.2d 1276, 1310, ¶ 51 (1983). The CPA attempts to distinguish Computer II on the grounds that it involved "millions of units of obsolescent equipment" and that transfer at net book "did the ratepayers a favor." CPA at 18. By contrast, argues the CPA, transfer of payphone assets at net book value would give LECs an unfair competitive edge. Id. But the Commission's rules governing asset valuation do not hinge on the relative obsolescence of the assets to be reclassified. And in any event, LECs will be reclassifying thousands of dumb payphones, which are increasingly obsolete.

Worse yet, it would prove an administrative nightmare: The Commission essentially would become a fence -- selling trucks, pedestals and all other manner of equipment illegally appropriated from the RBOCs to the highest bidder And contrary to the GPCA's suggestions, the Commission has no particular expertise in this area: Selling an entire ongoing business and all of its assets is a far cry from auctioning off blocks of spectrum.

The real motive of those commenters advocating a going-concern valuation is to distort competition in the nascent payphone market by saddling LEC payphone operations with artificial costs. This will force LECs to charge higher rates and create a price umbrella beneath which independent PSPs can price. See CPA at 18 (FCC should establish a high price-floor that will require the LECs to price their payphone-based services above their relevant costs). But such an anticompetitive distortion of the payphone market would only undermine the Act's pro-competitive promise and harm consumers, forcing them to pay more than they should for the same services. For these reasons, the Commission should reclassify LEC payphone assets using the Commission's traditional and time-proven net book valuation. See Exhibit A at 3.

Finally, in addition to identifying the valuation method, the Commission must identify the universe of assets that will be reclassified. Here too the Commission should continue to follow the course established in the inmate services proceeding and require LECs to reclassify only those assets already contained in their accounts.[17] It would make no sense for the Commission to create and reclassify assets not currently on the LECs' books, such as the existing contracts with location providers and alleged up-front bonuses. See CPA at n.18; Comments of the Inmate Calling Serv. Providers Coalition at 19-20 ("ICSPC"); South Carolina PCA at 7. None of this

[17]See Declaratory Ruling, Petition for Declaratory Ruling by Inmate Calling Services Providers Task Force, RM Docket No. 8181, at 13, ¶ 27 (Feb. 20, 1996) ("LECs must reclassify any inmate-only pay telephone investment recorded in Account 32.2351, Public Telephone Terminal Equipment").

is, or ever has been, an asset on the RBOCs' books. There is simply no reason to create a new special accounting rule for this proceeding.

III. NONSTRUCTURAL SAFEGUARDS EQUIVALENT TO THOSE PROVIDED IN COMPUTER III ARE SUFFICIENT FOR PAYPHONE DEREGULATION

The Coalition renews its support for the Commission's tentative conclusion to apply the Computer III (CC Docket 90-623) nonstructural safeguards to RBOC-affiliated PSPs. These safeguards have proven effective in policing anticompetitive cross-subsidization, as affirmed by state regulators in this very proceeding. The California Public Utilities Commission, for instance, states that the non-structural, Computer III safeguards "have proven successful" and "California supports them." CalPUC at 17.

Notwithstanding the Act's express mandate that the Commission use non-structural safeguards, some commenters argue for a structural separation requirement. But there is no reason to impose such a requirement, and every reason not to. Where it is prudent to operate payphones on an integrated basis, the LECs must be permitted to do so. And structural separation certainly is not necessary to ensure "that a LEC pay phone will be faced with the same opportunities and challenges that a PSP pay phone is faced with," as some independent PSPs contend. ACTEL at 9. Nor will a PSP be able to reap benefits from any affiliation with a LEC. As the Coalition explained in its opening comments (at 37-40), existing accounting safeguards and price-cap rules adequately ensure against cross-subsidy from regulated to unregulated operations. This Commission, the courts, and the Department of Justice have repeatedly so found.

The Coalition has supported the Commission's tentative decision to unbundle and tariff the two types of coin lines used by LEC PSPs -- the standard central-office coin line and the alternate ("smart set") access line. These two types of coin lines will generate competitive parity by enabling any PSP to use that coin line best suited to its payphones and the functionality it requires. AT&T goes much further and argues that LECs should be required to unbundle central office coin services (including coin recognition and answer detection) and central office coin transmission services (including access to the intelligence required to perform answer supervision, collect refund, far end disconnect and call timing). This abstract demand cannot be addressed in this proceeding. For one thing, very few non-LEC PSPs use central-office intelligence for these features, drawing into question the economic advisability -- the efficiency -- of engaging in such extensive unbundling in the absence of demonstrated demand.[18] Unbundling is often prohibitively expensive or economically infeasible.[19] As a result, unbundling requests should be judged on an ongoing and individualized basis under the three-part test set out in Computer III.[20]

Some commenters also propose other schemes to stifle the payphone industry under a heavy blanket of regulation. The APCC, for instance, proposes that all PSPs contribute to a "self-enforcement fund," with inspections, complaint investigation and other functions to be administered by an entity chosen by the Commission. APCC at 52. But APCC offers no

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[18]The Coalition estimates that in those regions offering both the standard coin line and the alternate access line, non-RBOC PSPs have chosen to install fewer than 5,000 central-office-implemented payphones using standard coin lines, while over 250,000 instrument implemented payphones use alternate access lines in those same regions.

[19]For instance, the GPCA requests that the LECs provide functionality that allows call rating to be programmable based on the subscriber's specifications. GPCA at 7. Some LEC switches, however, can handle only a single rate table. As a consequence, a coin line provided by these LECs would not allow private pay telephone providers to select their own rates. See, e.g., Comments of Ameritech at 18.

[20]Report and Order, Amendment of Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), 104 F.C.C 2d 958, 1065, ¶ 217 (1986) (decision to unbundle should be based on "the expected market demand for such elements, their utility as perceived by . . . competitors, and the technical and costing feasibility of such unbundling."), vacated on other grounds, California v. FCC, 905 F.2d 1217 (9th Cir. 1990), on remand, 6 FCC Rcd 7571 (1991).

indication that the Commission is incapable of handling complaints itself, and does not identify the unbiased agency that can handle that function in the Commission's stead. Likewise, the New Jersey Payphone Association (at 15) argues that non-discrimination obligations are insufficient and suggests that LECs should be required to provide service on terms deemed more desirable by the independent PSP. This proposal, however, has no statutory basis. Moreover, like APCC's suggestion, it would just add an additional layer of regulation that duplicates the protections already provided by the Commission's complaint process.[21]

Finally, the ICSPC attempts to hold up a raft of alleged bad acts by the RBOCs, even though these issues were considered and rejected in the inmate services proceeding. This is nothing more than an attempt to muddy the waters by alleging behavior -- which the RBOCs dispute -- that is now prohibited under the Act in any event. For instance, the ICSPC claims that the RBOCs charged PSPs for LIDB validation on an on-line, real-time basis, but that there is no mechanism in place to ensure that the RBOCs charge themselves the same rates. ICSPC at 25. Under the Computer III safeguards, however, RBOC PSP affiliates will have to impute the same charges for LIDB queries that the RBOC charge independent PSPs.[22]

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[21]The GPCA also argues that the Commission should limit the volume discounts that a LEC may offer on payphone lines and that the largest discount be made available to anyone with 5 percent of the lines provided to the LEC PSP GPCA at 10. This condition is inefficient, anti-competitive, and unnecessary.

[22]The CPNI safeguards of Computer III would also prevent an RBOC from making unauthorized use of an independent PSP's CPNI. Under these rules, RBOCs cannot disclose or use the CPNI of independent PSPs without prior permission and most certainly cannot "prefer[] or discriminat[e] in favor of their own payphone service." Opticom at 10.

IV. THE COMMISSION SHOULD ADOPT A REASONABLE AND BALANCED APPROACH TO CARRIER SELECTION

A. Permitting RBOCs' Ability to Negotiate with InterLATA Carriers Serves the Public Interest by Promoting Competition and Preventing Price Gouging

Grasping for arguments with which to oppose giving RBOC payphone providers regulatory parity, independent PSPs and IXCs weave together a series of internally contradictory assertions. Independent PSPs confidently contend that RBOC PSPs, if permitted to negotiate for the selection of the OSP, will outbid them and deprive them of locations for their payphones. See, e.g., APCC at 42. Taking precisely the opposite tack, the interexchange carriers assert with equal confidence that RBOCs will deprive location providers of any commissions at all. See AT&T at 24-25. Finally, inserting yet another contradiction, the APCC argues that denying RBOCs the ability to negotiate for selection of the OSP does not affect the commission paid to the location provider and, as a result, does not disadvantage the RBOCs in any event. See APCC at 44.

That these commenters would raise three contradictory arguments (none of which is supported by the testimony of a competent economist) shows only one thing -- the utter lack of merit to any of them. Far from advising the Commission on how best to serve the public interest, these commenters have made naked pleas for protectionist regulation that will favor their particular interests.

Those commenters charged with protecting the public weal rather than their own pocketbooks -- state regulators -- overwhelmingly support regulatory parity for RBOC PSPs in the selection of OSPs. They recognize that consumers are best served by a level playing field among all industry participants. CalPUC at 18; Comments of State of Florida Pub. Serv. Comm'n at 8; Comments of Pennsylvania Pub. Ultils. Comm'n at 7; Comments of Texas Pub. Utils.

Comm'n at 1. The Commission too has recognized this. explaining that "regulatory parity is an important policy that can yield important pro-competitive and pro-consumer benefits." Report and Order on Reconsideration, Petition of Arizona Corp. Comm'n to Extend State Authority Over Rate and Entry Regulation of All Commercial Mobile Radio Services, 10 FCC Rcd 7824, 7833 (1995). And Congress recognized this principle in Section 276 itself, placing the burden of proving public harm on those who oppose regulatory parity in the payphone context.[23] Even Sprint favors regulatory parity, noting that the RBOCs "will be unduly hampered in their ability to compete with PPOs" if they do not have "the same right that private payphone providers have to select and contract with the presubscribed interLATA carriers for their payphones." Sprint at 29.

Thus, once one focuses on the public interest rather than the private interests of a select few, it is clear that permitting RBOCs to negotiate with location providers regarding carrier selection is desirable. It not only promotes the public interest in competition but also helps protect consumers from "gouging" by unscrupulous OSPs. As the Coalition has pointed out, established organizations like the RBOCs, with service reputations to protect, are exceedingly unlikely to select a price-gouger as the OSP.[24]

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[23]While some opponents of regulatory parity argue that the Commission may allow the RBOCs to negotiate with the interLATA carrier "if -- and only if -- the Commission determines that such RBOC negotiations with location providers would serve the public interest," see Comments of Oncor at 3, they have it backwards. Under the plain language of the statute, the opponents of regulatory parity bear the burden of proving that parity would be against the public interest. This is a burden they cannot meet.

[24]It is therefore unsurprising that high-priced OSPs oppose RBOC participation in carrier selection. Permitting RBOCs to select the OSP for their phones will substantially reduce gouging, lower the number of complaints before the Commission, and make proceedings such as CC Docket No. 92-77 (Billed Party Preference for InterLATA 0+ Calls) moot.

Seeking to elevate its own interests over those of the public, AT&T argues that, if the RBOCs are permitted to negotiate with site providers, they will deny location providers commissions altogether. See AT&T at 24-25. Indeed, AT&T appears to have mounted a massive letter writing and disinformation campaign -- which began when the Telecommunications Act was only a bill (see Exhibit B) -- to convince location providers that their commissions are at stake. But neither AT&T nor the location providers provide any explanation as to how permitting the RBOCs to negotiate with location providers concerning selection of the OSP could hurt the location provider, especially where the location provider retains ultimate control over the selection.[25]

Indeed, it is quite clear that the prohibition against RBOC involvement in the OSP selection process hurts location providers. As the APCC points out, location providers -- who often receive no commissions from OSPs today -- might well receive higher commissions if RBOCs are permitted to negotiate with OSPs on their behalf. See APCC at 42 (arguing that RBOCs might demand higher "commission levels" from carriers which can be used to "bid up location provider commissions"). Clearly, AT&T does not wish to compete against RBOC PSPs on the basis of commissions -- or to face RBOC PSPs, acting on behalf of location providers,

[25]The choice of IXC is subject to negotiation between the parties, just like any other term of the agreement. Neither the location provider nor the PSP need enter into the contract if they object to the choice of IXC. S. Conf. Rep. 230, 104th Cong., 2d Sess. 159 (1996) ("Location providers . . . have control over the ultimate choice of interLATA and intraLATA carriers in connection with their choice of payphone service providers"). Consequently, the argument that RBOC PSPs will threaten to remove payphones if location providers don't choose their preferred IXC, Oncor at 3, is without merit. This is a competitive market; if the RBOC PSPs were to do so, other PSPs will offer better terms and replace them. It therefore comes as no surprise that competing PSPs do not argue that RBOC PSPs will pay too little compensation; they fear that the RBOC PSPs will pay too much. See APCC at 42. Moreover, non-RBOC PSPs could do the same thing, as the one instance of a supposed threat cited by AT&T (on information and belief) -- a threat allegedly issued by the non-RBOC PSP, Citizens Telecom -- demonstrates. See AT&T at 25.

in commission negotiations.[26] But naked protectionism for an industry giant like AT&T simply cannot be justified under the rubric of public interest.

APCC, for its part, now uses the possibility of greater commissions as a justification for saddling RBOC PSPs with a series of onerous regulatory restrictions. According to the APCC, if RBOC PSPs use payphone aggregation to obtain higher commissions from OSPs, they might use "the additional funds . . . to bid up location provider commissions to unparalleled levels, effectively foreclosing IPP providers from competing for profitable locations." APCC at 42; see also Comments of Worldcom, Inc. at 22. In essence, APCC argues that access to large amounts of capital will permit predatory purchasing of payphone sites at supracompetitive prices. But this theory makes no economic sense. Such predation is impossible unless there is a mechanism for recouping the initial losses (in this case, the cost of supposedly excessive commissions paid to location providers). Because the payphone market is competitive and there are low barriers to entry, RBOC PSPs could never reduce commissions below competitive levels so as to recover their losses; new entry would undermine any such attempt. As a result, the hypothetical predation scenario posited by the APCC must be dismissed for what it is -- a pseudo-economic fantasy spun out by yet another special interest seeking protectionist regulation.[27]

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[26]As the APCC explained to Congress, AT&T would be "crazy" not to oppose this relief, precisely because it is fair: "[T]his provision allows for parties of equal negotiating power to square off against each other. Instead of AT&T negotiating with the local convenience store or mall owner, the House provision permits the RBOCs to obtain location providers' authority to aggregate the location providers' RBOC payphones with other payphones to negotiate head-to-head with the large carriers to determine which of these carriers will provide interLATA service from RBOC payphones. At the same time, as we have repeatedly stated, the location provider retains the ultimate choice of interLATA carrier by virtue of controlling the telephone." Memorandum from Mark Paoletta and Albert H. Kramer to Republican Staff at 2 (Oct. 16, 1995).

[27]Similarly unsupported is the suggestion that IXCs will somehow be victimized by RBOC PSPs and be forced to raise their rates as a result. For example, AT&T argues that RBOCs will "extract extraordinary commissions from IXCs," thereby "add[ing] to the costs that consumers

Moreover, the regulatory "solutions" proposed by APCC (at 43-44) and the California Payphone Association (at 20), which limit either the portion of interLATA traffic an RBOC can deliver to any particular carrier (e.g., 25%) or the number of payphones or calls that must be aggregated to receive an interLATA IXCs's highest available 0+ commission level (i.e., a rate cap on IXC commissions), are blatantly anticompetitive.[28] If economies of scope and scale permit RBOCs to negotiate better deals on behalf of location providers, there is no sensible reason to prohibit them from doing so. The Commission has consistently rejected the imposition of such protectionist restrictions in the past.[29]

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must bear . . . ." AT&T at 25-26; see also Comments of Competitive Telecommunications Ass'n at 20 ("the BOCs could demand terms and commissions from IXCs seeking to serve the payphones"). But this makes no sense whatsoever. The interexchange market is enormous -- over 67 billion dollars -- and RBOC PSP purchasers are just a small part (1.9 billion) of that market. The suggestion that RBOC PSPs might exercise power in this market and force prices upward is thus utterly senseless. Memorandum Opinion and Order, Applications of Craig O. McCaw and AT&T, 9 FCC Rcd 5836, 5847, ¶ 14, 5856, ¶ 30 (1994) (rejecting market defined as cellular interexchange market, and holding that competitive effect of merger would be negligible because McCaw held only a small portion of total interexchange market). AT&T's further assertion -- that increased commissions would "reduce the number of carriers that will be available from payphones on a 0+ basis" -- is simply bizarre. Since each payphone is capable of having only one 0+ carrier, how the number of available carriers could be "reduce[d]" -- to zero perhaps? -- is a true mystery.

[28]The APCC's suggested approach is the most restrictive of all. It would limit the amount of interLATA traffic that an RBOC could deliver to any one IXC to one-third of the percentage of non-RBOC payphones in the area. Thus, an RBOC with competitors that have 43% of the market would be permitted to deliver only 14% of its traffic to any one IXC, effectively requiring the RBOC to use 5 different IXCs. A higher RBOC share (e.g., 70%) would require 7 different IXCs. On top of that, the APCC would require complete structural separation and a limit on amount of traffic a RBOC could send to its own IX affiliate.

[29]See, e.g., 9 FCC Rcd at 5860, ¶ 35 (refusing to place restrictions on AT&T cellular operations for the sole purpose of subjecting them to the same restrictions as competing RBOC cellular companies). The fact that some competitors (non-RBOC PSPs) have not yet achieved certain efficiencies enjoyed by others (the RBOC PSPs) is no reason to deny those efficiencies to all.

AT&T attempts to condition relief here on the RBOCs' prior authorization to provide in-region interLATA services. See AT&T at 24 (arguing that parity would be the equivalent of allowing RBOCs "to enter the interLATA market through acquiring an economic interest in . . . the IXCs they designate to serve those payphones," which cannot occur "before the BOCs are permitted to enter the in-region interLATA market pursuant to Sections 271 and 272 of the Act"). But this theory cannot find any support in the statute, which allows for Section 276 relief without prior Section 271 approval. In this sense, the RBOCs' ability to participate in the IXC selection process is no different than their newly granted ability to provide interLATA wireless and information services, neither of which are tied to section 271 relief. Sprint (at 29) agrees.

Alternatively, AT&T urges the Commission not to permit RBOC participation until further proceedings are completed. But this is nothing more than a strategy of delay. Bob Allen has publicly proclaimed: "[I]t could be well into the next century before any of [the BOCs] serve their first long-distance customer in their own territory . . . We didn't send our lawyers on vacation. . . . We are already bird-dogging the FCC and the state regulatory commissions." John J. Keller, AT&T Challenges the Bell Companies, Wall Street Journal, June 12, 1996, at A3. AT&T is doing just that here -- bird-dogging the Commission in an attempt to forestall competitive entry. Congress set a November deadline for implementation of Section 276. None of AT&T's arguments warrant disregard of this congressional command.[30]

[30]MCI argues that until the RBOCs face significant competition in the local exchange market, they will be able to subsidize commission payments to premises owners with regulated service revenues. MCI at 19. But the elimination of payphone subsidies is one of the primary purposes of Section 276, and MCI makes no showing that the Commission's accounting and price-cap safeguards are insufficient for that task. Moreover, MCI offers no reason why allowing RBOCs to negotiate with OSPs increases the likelihood of cross-subsidies, since the same incentive (or lack of incentive) to cross-subsidize exists whether or not RBOC PSPs participate in negotiations.

Finally, APCC argues that relief is unnecessary in any event. See APCC at 44. "[T]he BOCs suffer no disadvantage by not being able to choose the presubscribed interLATA OSP," the APCC asserts, because the location providers using RBOC phones can negotiate for commissions directly with the interLATA OSP. But the APCC itself demonstrates that this argument is wrong. According to the APCC, PSPs that aggregate payphones can negotiate better commissions from OSPs. Id. at 42. Currently, non-RBOC PSPs can aggregate their payphones and obtain those increased commissions for their customers. Competing RBOC PSPs are at a disadvantage because they cannot. Moreover, the APCC refuses to admit that location providers prefer and often require one stop-shopping that, absent competitive parity, RBOCs cannot provide. By denying that these disadvantages exist, APCC and its members seek to perpetuate them.

In the end, APCC's opposition to parity is not only a self-serving attempt to foist a regulatory disadvantage on its competitors, but a cynical and hypocritical example of regulatory gamesmanship. Before Congress, when it supported legislation that would benefit its members in many respects, the APCC repeatedly admitted that the inability to negotiate for selection of the OSP put RBOCs at a disadvantage, referred to the restriction as "arbitrary," and repeatedly urged Congress to correct the imbalance. See Letter from Albert H. Kramer, Attorney for the APCC, to the Hon. Larry Pressler, at 1-2 (June 2, 1995) (urging Congress to allow RBOCs to select interLATA carriers on their payphones because it "provide[s] a basis upon which all industry participants compete on equal terms"); Letter from Albert H. Kramer, Attorney for the APCC, to the Hon. Larry Pressler, at 2 (May 16, 1995) (urging the removal of restrictions on RBOC carrier selection because it "provides for a competitive environment in which all competitors compete on equal terms"); Memorandum from Mark Paoletta and Albert H. Kramer to Republican Staff at 2 (Oct. 16, 1995) (urging Congress to adopt the regulatory parity provision despite IXC opposition because the "legislation is intended to make the marketplace competitive by removing arbitrary restrictions, such as this restriction, on the RBOCs, and not to satisfy any one particular industry").[31]

Now that the statute has passed and regulatory parity is around the corner, APCC is suddenly arguing the opposite to the Commission, seeking special protection for its members instead. It seems that, like the young St. Augustine and virtue, the independent PSPs pray for competition -- but not just yet. Competition, however, need brook no more delays. As the APCC itself explained to Congress, the purpose of this legislation is to "make the marketplace competitive by removing arbitrary restrictions, such as this restriction, on the RBOCs" -- "not to satisfy any one particular [segment of] industry." APCC Memorandum of Oct. 16, 1995, at 2.

B. PSPs' Ability to Negotiate with IntraLATA Carriers and Dialing Parity

At the same time they seek to deny RBOC PSPs the right to participate in the selection of the interLATA carrier on RBOC payphones, the APCC and the interexchange carriers are adamant that they be given the unfettered ability to select the intraLATA carrier on their payphones. Notwithstanding the selectivity with which these participants invoke competitive parity, the Coalition agrees with the APCC that the Commission must make "the right" of PSPs to choose a qualified intraLATA carrier for all calls "explicit." APCC at 41.

Some carriers, however, go further than the public interest demands or the statute will allow. For example, AT&T asks the Commission to "consider requiring immediate intraLATA presubscription for all [R]BOC payphones which are located in territories where intraLATA presubscription is technically available." AT&T at 28 n.51. But mandatory intraLATA dialing

[31]For the Commission's convenience, BellSouth has submitted these letters as an attachment to its Reply Comments.

parity has no basis in Section 276 and cannot be implemented for intraLATA payphone calls apart from intraLATA business and residential calls. Accordingly, while the Commission must permit PSPs to select any intraLATA carrier they choose, it should affirm that, until such time as intraLATA dialing parity/presubscription is available for all phones in a particular state, PSPs should use their "smart" payphones to direct calls to their chosen intraLATA carrier.

C. Treatment of Existing Contracts

Several parties have urged the Commission to abandon the plain text of the statute and adopt a strained and unnatural reading of "contract" that better serves their interests.[32] But as Sprint correctly recognizes "a contract, to be grandfathered, must contain binding obligations applicable to both parties." Sprint at 30. A simple LOA authorizing an IXC to make a PIC change, having no mutuality of obligations (e.g. no agreement by the premises owner to subscribe to the IXC's service for any fixed length of time) should not be regarded as such a contract. Indeed, it is standard industry practice for IXCs to solicit each others' clients and urge them to sign a new LOA. If LOAs were binding and inviolate contracts, this practice (which the Commission has approved so long as the means are fair[33]) would amount to tortious interference with contractual relations. Thus, Oncor is simply wrong to argue (at 14) that LOAs are binding on both premises owner and IXC; nothing in a LOA between a subscriber and a carrier prevents

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[32]See Airports Council International -- North America at 4 (urging the Commission to adopt "the broadest possible definition of 'contract,' including letters of authorization and term extensions, so as not to disadvantage location providers, such as airports, that may rely on existing presubscription agreements for a necessary income stream."); AT&T at 27 n.50 ("The definition of 'contract' for these purposes should include all agreements or authorizations which commit a location owner to select a particular IXC for phones at its premises. This would include lawfully executed letters of authorization, as well as all other lawful agreements.").

[33]See Report and Order, Policies and Rules Concerning Unauthorized Changes of Consumer Long Distance Carriers, FCC No. 94-129, CC Docket No. 94-129 (June 14, 1995) (proscribing misleading practices with respect to LOAs).

the subscriber from changing its chosen carrier. This, however, must be distinguished from cases in which the premises owner has signed a LOA permitting the PSP to select the carrier. In such a case, the LOA is enforceable against the premises owner and forms part of the contractual relationship between them.[34]

V. THE COMMISSION SHOULD ENSURE THAT PUBLIC INTEREST PAYPHONES ARE FINANCED BY THE REQUESTING ENTITY

Finally, in promulgating any regulations concerning public interest payphones, the Commission must recognize that the provision of public interest payphones varies dramatically around the nation. Thus the California system, while workable there, see CPA at 24, does not provide an appropriate solution for other states, which may well have different competitive conditions and larger percentages of public interest payphones.

Consequently, California's scheme should be grandfathered, but public interest payphones in other states should be paid for by the requesting entity. The CPA concedes that this is a workable solution, and it has proven effective in Iowa. CPA at 14. See Iowa Utility Board at 4 ("If a community was concerned about keeping a payphone in the community, the community could provide it. This solution appears to be acceptable. In the eleven years that payphones have been deregulated the issue has arisen very rarely at the agency or legislative level."); see also Comments of Vermont at 11 ("It is also appropriate that responsibility for funding public interest payphones fall upon the party that prescribes any siting standards.").

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[34]GPCA's suggestion that there should be a "fresh look" at contracts entered into between enactment of the legislation and implementation of the Commission's rules finds no basis in the statute. Such contracts are not expressly grandfathered, but they are still valid contracts and there is no reason to abrogate or even question them. See Bell Telephone Co. of Penn. v. FCC, 503 F.2d 1250, 1280 (D.C. Cir. 1974) ("The Communications Act contains no express statement of an intention to authorize unilateral modification or abrogation of privately negotiated contracts"), cert. denied, 422 U.S. 1026 (1974).

CONCLUSION

The Commission should ensure that all PSPs are operating on an even playing field so that competition is allowed to flourish. It should allow RBOC PSPs, like their independent counterparts, to be involved in the IXC selection process. It also must remove payphone assets from carrier access charges and reclassify RBOC payphone assets to nonregulated assets. In so doing, the Commission should follow its precedents and reclassify the payphone assets at net book value; moreover, it should only reclassify assets actually on the RBOCs' books. And, most importantly, the Commission should take advantage of existing market-based proxies when prescribing regulations that guarantee PSPs compensation for each and every call made using their payphones. Only by relying on existing market-tested experiences in this fashion will the Commission erect the "pro-competitive, de-regulatory national policy framework" envisioned by Congress.

Respectfully submitted,

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July 15, 1996

ANDREWS OFFICE PRODUCTS CAPITOL HEIGHTS, MD (K)

Exhibit A

Critique of MCI's Use of the Hatfield Study and Other Issues

Carl R. Geppert

July 15, 1996

Arthur Andersen LLP ("Arthur Andersen") was asked to address three issues in this Reply Report. Section I of this report critiques MCI Telecommunications Corporation's ("MCI's") use of the October 10, 1995 "Payphone Compensation Cost Analysis" prepared by Hatfield Associates, Incorporated ("Hatfield"). Section II addresses concerns raised regarding the reclassification of payphone assets to nonregulated activities. Section III recalculates the "completed call" 0- transfer charge (included in our previous report) using updated 0- transfer charges.

SECTION I: CRITIQUE OF MCI'S USE OF THE HATFIELD STUDY TO QUANTIFY PAYPHONE COMPENSATION

MCI believes that Payphone Service Providers ("PSPs") should be compensated at a rate of $0.083 per access code call. To support this theory, MCI relies upon an October 10, 1995 Hatfield study ("the Hatfield Study"), initially prepared in response to CC Docket No. 91-35. We believe it is inaccurate to use the results of this study as a basis for "fair compensation" to PSPs as dictated by Section 276 of the Telecommunications Act of 1996 ("the Act"). There are four problems with this approach.

First, the Hatfield Study is not intended to calculate the cost of providing payphone service. The Hatfield study simply estimates the cost of installing and maintaining one additional coinless, indoor payphone in the state of New Hampshire, assuming a base of payphones is already in operation. The following is a brief list of additional cost categories that should be considered were the Hatfield Study to be used in computing the cost of providing payphone service.

- Local Usage Charges
- Coin Collections
- Forecasting and Budgeting
- Product Management
- Marketing, Advertising & Sales
- Business Office
- Real Estate Management
- Financial Management
- Legal Services
- Recurring Revenue

Second, the Hatfield Study is not applicable to the mix of Coalition payphones. The type of payphone used in the Hatfield Study (i.e., coinless, indoor) accounted for only 5.9% of the entire New Hampshire payphone base. Coalition-provided data suggests all coinless payphones account for only 6.6% of the Coalition payphone base[1].

Third, the Hatfield Study contains numerous inaccuracies in attempting to calculate the cost of installing and maintaining the average payphone. The following list illustrates this point.

1. Payphone Cost: MCI, through the use of the Hatfield Study, believes that compensation should be, in part, based upon the purchase price and installation costs of coinless, indoor payphones in the state of New Hampshire (i.e., $300.39). This assumption raises two concerns. First, the coinless, indoor payphone was the second least expensive of the payphone inventory maintained by New England Telephone - New Hampshire ("NET-New Hampshire"). In fact, the range of payphone costs spanned from $1,324.56 to $247.22. Second, the $300.39 used in the Hatfield Study includes only $12.98 in set costs. The "incremental" New Hampshire sets were presumed to be taken from a near fully depreciated inventory of excess coinless phones. This is certainly not applicable to Coalition members who do not have fully depreciated sets in inventory.

2. Maintenance: MCI inappropriately assumes that the cost of maintaining a coinless payphone in NET-New Hampshire ($38.18) can be used as a surrogate to derive compensation on Coalition calls. The NET study, in fact, computes the average maintenance cost for public payphones to be $197.91. If you include semi-public payphones, the average dips to $166.05. Moving out of New Hampshire, where it is presumed, for example, that payphones in Los Angeles, Chicago and New York City have higher call volumes than payphones in New Hampshire, the cost of maintaining payphones increases.

3. Business Line: It appears as though the average 1994 business line figure used in the Hatfield Study ($320.28 per year) is inappropriate. As stated in Nynex Telephone Companies' ("Nynex") reply comments to CC Docket 91-35, New Hampshire's business line costs were $525.

[1] Ms. Mary J. Sisak, in her attachment to MCI's comments, attempts to justify the Hatfield Study's use of the indoor, coinless payphones as a surrogate for all payphones by saying, "Most private payphones, however, are in airports, hotels and other controlled environments..." (i.e., they are indoor). Her explanation, however, does not support the basis for using coinless payphones, nor does it justify the Hatfield Study's applicability to Coalition members.

4. Commissions: The Hatfield Study excludes the cost of commissions that PSPs pay (or would have to pay) to premise owners for the use of their property. This cost is essential to the provision of payphone service, is incremental in nature and is generally accepted as a component of incremental cost studies.

Fourth, the Hatfield Study inappropriately includes local sent paid calls when computing the average number of calls per coinless payphone. Coinless payphones cannot carry local sent paid calls.

After correcting the Hatfield study for all of the issues noted above (using Coalition-provided data for payphone, maintenance, business line, commissions, coin collections and joint and common costs as well offsetting recurring revenue figures), the revised per-call cost is $0.306. This figure should be compared to the overall average cost of $0.29 computed in our earlier submission.

The $0.306 per-call cost computed above is supported by other cost studies. For example, the staff of the Illinois Commerce Commission ("ICC") calculated the annual incremental cost of operating a payphone station, excluding common expenses, to be $89.92 per month[2] or $1,079.04 per year. With common costs added to the station cost, the ICC concluded that the average cost per call is approximately $0.30[3].

SECTION II: RECLASSIFICATIONS OF ASSETS AT GOING CONCERN VALUE OF PAYPHONE OPERATIONS

Certain comments have suggested that LECs should transfer their payphone operations to nonregulated activities at the going concern value of the payphone operations or at net book value plus the market value of their existing payphone contracts. As stated in our July 1, 1996

[2] See AAA Coin-Phones & Systems, Inc. et al. v. AT&T, et al., Complaint for Just and Reasonable Compensation for Billable Operator, 800, 900, and 700 Service Calls, Illinois Commerce Commission, Docket No. 92-0400, Order, issued October 3, 1995, at 12.
[3] Id, at 18.

report, the reclassification of payphone assets should be limited to specific tangible assets. The use of a "going concern" value or "contract values" would most certainly incorporate intangible values. Creating intangible assets as a result of an asset reclassification between two affiliated entities has never been required or allowed in any FCC proceeding. Therefore, we believe that the asset reclassification amounts, consistent with prior practice, should be limited to tangible assets, and should be reclassified at net book value.

SECTION III: REVISED 0- TRANSFER CHARGE STUDY

We have revised our earlier calculation of the "completed call" 0- transfer study using updated 0- transfer charges. The revised range of 0- transfer charges for the entities listed in the Second Report and Order is \$0.28 - \$0.46, the simple average of these two figures being \$0.37. After applying the call completion ratios described in our earlier report (approximately 69% to 81%), the updated/revised 0- transfer charge for "completed calls" ranges from \$0.46 - \$0.54.

ARTHUR ANDERSEN LLP

by Carl R. Geppert [signature]

Carl R. Geppert

Exhibit B

AT&T

Suite 200
5501 LBJ Freeway
P. O. Box 650345
Dallas, Texas 75265-0345

October 5, 1995

Dwayne Miller
Jail Administrator
200 South McDonald
McKinney, TX 75069

Dear Dwayne,

Very soon the House and Senate will begin Conference Committee debates on H.R. 1555, the Barton Amendment. This proposed legislation contains provisions which will affect your current public and inmate telephone arrangement. The legislation may prevent premise owners from receiving any commissions. In addition, it may also affect the amount and level of public and inmate telephone service you are able to provide.

The Barton Amendment would allow the Regional Bell Operating Companies (RBOC's) to choose the long distance and local service provider on all inmate and public telephones they have installed on agent properties—yours included! The RBOC's currently own over 85% of the public telephones installed and this gives them an unfair competitive advantage. Where competition is limited or practically non existent, the impetus to pay commissions disappears. The RBOCs may also limit the amount of equipment or service they provide

We urge you to contact the House and Senate members on the attached list, *as soon as possible*, to voice your opposition to this legislation. We have attached a sample letter that may assist you in this endeavor. Should you have any questions please contact me on (800) 848-6235. Thank you for your prompt response.

Sincerely,

Dean Ramsey

Dean Ramsey
Account Executive

Attachments

SAMPLE LETTER

Date

Name and Address of
House/Senate Committee Member

RE: H.R. 1555-- The Barton Amendment

Dear Congressman/Representative or Senator:

It has come to our attention that a House Bill currently under debate by both the House and the Senate contains a provision which will negatively impact our ability to provide pay telephone service to the public and our inmates from our property (ies). Provisions in the Barton Amendment would give the Regional Bell Operating Companies (RBOC's) the right to select the intraLATA and interLATA service provider from RBOC owned phones.

We strongly oppose this provision of H.R. 1555. We view this as an opportunity to give the RBOC's an unfair competitive advantage. The RBOC's own over 80% of the public payphones. Taking the choice away from the premise owners and giving this choice to a few is not the way we expect Washington to respond to this industry. We expect to receive the best possible service, at the best price, with the best possible return to our taxpayers. The RBOC's would be in a position to decide how where and at what cost public and inmate telephone service is available.

The RBOC's would, in effect, be deciding what is best for our customers and inmates. In fact, we have studied long and hard to determine what our public telephone needs are. The health / competition in the current public and inmate phone environment allows us to secure high quality, innovative telecommunication service. Please do not remove this competition. Keeping the right to choose our carrier(s) ensures service at a reasonable cost to the taxpayers and in a ubiquitous manner.

We are very much opposed to H.R. 1555 and we urge you to oppose it in conference.

Sincerely,